No. 89-1910

IN THE

Supreme Court of the United States

OCTOBER TERM, 1990

JOANNE LIMBACH,
TAX COMMISSIONER OF OHIO,
Petitioner,

v.

AMERICAN HOME PRODUCTS CORPORATION,
Respondent.

On Petition for Writ of Certiorari to the Supreme Court of Ohio

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BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

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QUESTION PRESENTED FOR REVIEW

Whether the income earned by a corporation from the investment of funds that are not held for use as working capital in, or otherwise connected with, that corporation's business operations constitutes unitary business income that may be apportioned to the States in which the corporation does business.

LIST OF PARTIES

The petitioner in this case is Joanne Limbach in her official capacity as Tax Commissioner of Ohio. The respondent is American Home Products Corporation.

Pursuant to Supreme Court Rule 29.1, the Court is advised that American Home Products Corporation has no parent corporation. It does, however, have a number of wholly-owned subsidiaries and the following subsidiaries that are not wholly-owned: Nippon Sherwood Co. and Wyeth-Ayerst Pharmaceuticals, Inc.

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STATEMENT

American Home Products Corporation ("AHP") is a Delaware corporation with headquarters in New York City, and during the years in issue was primarily engaged in the business of manufacturing and marketing prescription drugs, medical supplies, packaged medicines, foods, household products, and housewares. As part of its operations, AHP engaged in manufacturing and sales activities in the State of Ohio. These activities obligated AHP to pay Ohio franchise tax on its net income during

tax years 1980 to 1983, the period at issue in this case. *See* Ohio Rev. Code §§ 5733.01(A), 5733.06.

AHP's operations over this period were profitable, generating a substantial amount of excess cash. Due to uncertainties in the capital and equity markets, AHP invested these funds in a variety of short-term instruments. Only a portion of these accumulated funds were needed as working capital in AHP's operations; the remainder represented an investment fund. These investments were managed from AHP's New York headquarters and the securities themselves were stored in a vault at a New York bank.

Ohio's franchise tax scheme relies on the "unitary business" principle and formula apportionment. Under this system, any income produced by property located in Ohio is allocated to Ohio to calculate the tax. *Id.* § 5733.051. The remainder of the taxpayer's unitary business income is apportioned through application of a formula based on the property, payroll, and sales attributable to Ohio. *Id.* § 5733.05. In preparing its franchise tax returns for tax years 1980 through 1983, AHP applied a formula to calculate the portion of its interest income that was attributable to the funds held as working capital and the portion that was attributable to the funds held for investment. Only the former was included in the income to be apportioned to Ohio.

Petitioner, the Ohio Tax Commissioner, audited AHP's 1980 to 1983 franchise tax returns and took the position that all interest income, even that attributable to funds held solely for investment rather than for working capital, should be apportioned. AHP appealed to the Ohio Board of Tax Appeals, arguing that the income on the investment funds was non-unitary and thus under the Due Process Clause was not constitutionally subject to taxation in Ohio. Alternatively, AHP argued that the manner in which the Tax Commissioner had apportioned the income was incorrect under the statute.

The Board of Tax Appeals found that the investment portion of AHP's fund was managed and controlled exclusively from New York and that the interest income was "generated entirely outside Ohio." App. to Pet. at A-12. The Board of Tax Appeals also found that these investment activities were independent from AHP's other businesses since the investment fund was not used in any fashion as a source of working capital. *Id.* at A-10, A-12. These factual findings led the Board of Tax Appeals to agree with AHP that there was insufficient nexus between AHP's business in Ohio and the income on AHP's investment funds to subject that income to taxation in Ohio. As an administrative tribunal, however, the Board of Tax Appeals concluded that it lacked authority under Ohio law to rule on the constitutional validity of the statute requiring taxation of such income. The Board of Tax Appeals went on to reject AHP's alternative statutory argument, and therefore affirmed the assessment.

Both parties appealed to the Ohio Supreme Court. Even though her assessment ultimately had been affirmed by the Board of Tax Appeals, the Commissioner challenged the Board's determination that Ohio had no nexus with the income on AHP's investment fund. AHP renewed its constitutional and statutory arguments. The Ohio Supreme Court applied this Court's decisions in *Mobil Oil Corp. v. Commissioner of Taxes*, 445 U.S. 425 (1980), and *ASARCO Inc. v. Idaho State Tax Comm'n*, 458 U.S. 307 (1982), and in a unanimous, per curiam opinion ruled that based on the factual findings of the Board of Tax Appeals, the income from the investment fund was not constitutionally subject to taxation in Ohio as part of AHP's business operations. The Ohio Supreme Court did not reach AHP's statutory argument. This petition followed.

ARGUMENT

Supreme Court review of this case is neither appropriate nor necessary. The Ohio Supreme Court merely has applied the legal standards contained in this Court's decisions to a particular, rather unique factual scenario. Such a factbound application of well-established law does not merit discretionary review, particularly since this Court already has indicated that state court applications of the relevant standards are entitled to substantial deference. Moreover, petitioner does not even allege any direct conflict in the lower courts on the issue presented. The reason for this failure is clear; the lower courts are engaging in the case-by-case assessment called for by this Court's jurisprudence and have reached decisions entirely consistent with that of the Ohio Supreme Court in this case. Finally, there is no need for review in this case because the Ohio Supreme Court's application of this Court's decisions is correct.

I. THE PETITION PRESENTS ONLY AN APPLICATION OF ESTABLISHED PRINCIPLES TO A PARTICULAR FACTUAL SETTING

"Various aspects of state tax systems based on the 'unitary business' principle and formula apportionment have provoked repeated constitutional litigation in this Court." *Container Corp of America v. Franchise Tax Bd.*, 463 U.S. 159, 163-64 (1983). Broadly stated, the issue presented in such litigation is reconciliation of the established due process principle that "a State may not tax value earned outside its borders," *ASARCO*, 458 U.S. at 315, with the "unitary business" principle, which calls for apportionment of the full income of a unitary business entity. In a series of decisions beginning with the 1980 Term, the Court has clarified the applicable constitutional standards. *See Mobil Oil Corp. v. Commissioner of Taxes*, 445 U.S. 425 (1980); *Exxon Corp. v. Wisconsin Dep't of Revenue*, 447 U.S. 207 (1980); *ASARCO Inc. v. Idaho State Tax Comm'n*, 458 U.S. 307 (1982);

F.W. Woolworth Co. v. Taxation & Revenue Dep't, 458 U.S. 354 (1982); *Container Corp. of America v. Franchise Tax Bd.*, 463 U.S. 159 (1983). As a result of these decisions, "[t]he legal principles defining the constitutional limits on the unitary business principle are now well established." *Container Corp. of America v. Franchise Tax Bd.*, 463 U.S. at 176.

Specifically, the Constitution places "certain constraints" on the States' ability to define a particular business as unitary:

> The Due Process and Commerce Clauses of the Constitution do not allow a State to tax income arising out of interstate activities—even on a proportional basis—unless there is a " 'minimal connection' or 'nexus' between the interstate activities and the taxing State, and 'a rational relationship between the income attributed to the State and the intrastate values of the enterprise.' ". . . In addition, the[se] principles . . . require that the out-of-state activities of the purported "unitary business" be related in some concrete way to the in-state activities.

Id. at 165-66 (citations omitted).

The Ohio Supreme Court expressly applied these principles, and this Court's decisions, in the case at hand. Relying primarily on *ASARCO*, 458 U.S. 307, the Ohio Supreme Court determined that AHP's activities in managing the investment fund were not related in a concrete way to the business AHP conducted in Ohio because the funds held for investment were not used to operate that business or as a source of working capital. *See* App. to Pet. at A-7. The Ohio Supreme Court found footnote 21 of *ASARCO* to be "pivotal." In that footnote, the *ASARCO* Court had noted that ASARCO's investments were not pledged to secure working capital or otherwise used in ASARCO's business operations, because the company had adequate, alternative sources of cash. These facts, the *ASARCO* Court indicated, rendered income from those investments outside ASARCO's unitary business

operations and beyond the taxing power of Idaho. 458 U.S. at 324 n.21.

Here, after noting that the issue was "factual," the Ohio Supreme Court similarly found that the investment portion of AHP's funds were not used as a source of working capital for AHP's other business operations. In making this ruling, the Ohio Supreme Court relied on a factual finding by the Board of Tax Appeals that AHP in no way used the investment portion of its funds as working capital in its business operations. This fact, together with the independent nature of AHP's investment activities and their lack of any other connection with Ohio, led the Ohio Supreme Court to conclude that AHP's income from the investment portion of its funds should not be apportioned.

In light of the careful approach taken by the Ohio Supreme Court, it is not surprising that petitioner does not argue that the Ohio Supreme Court applied the incorrect standards; petitioner simply disagrees with the result. The legal principles are—as this Court expressly stated in *Container Corp. of America v. Franchise Tax Bd.*, 463 U.S. at 176—"well established," and the petition only presents—as petitioner's own argument heading makes clear, *see* Pet. at 10—the question of whether the Ohio Supreme Court has "Misapplied This Court's Test Of A Unitary Business." Thus, the question petitioner seeks to present is not worthy of discretionary review.

In this case, moreover, there is an even more compelling reason to deny the petition. This Court has held that state court determinations as to the scope of a unitary business are entitled to substantial deference:

> [T]his Court will, if reasonably possible, defer to the judgment of state courts in deciding whether a particular set of activities constitutes a "unitary business."

Container Corp. of America v. Franchise Tax Bd., 463 U.S. at 175. Recognizing that the factual records in-

volved in applying constitutional principles to "unitary business" determinations "tend to be long and complex," this Court has expressed an intention not to review "every colorable claim that a state court erred in a particular application of those principles," but rather to accept state court judgments that are " 'within the realm of permissible judgment.' " *Id.* at 176 (footnote omitted). This deferential approach to state court applications of the law in this area makes the present case a particularly poor candidate for review.

In short, through a series of decisions this Court has clarified the legal standards controlling the issue petitioner seeks to present, and indicated that, even more than usual, the application of those principles—the only issue presented by the petition in this case—is to be left to the state courts. The petition therefore should be denied.

II. THERE IS NO CONFLICT IN THE LOWER COURTS

Petitioner does not allege any direct conflict over the application of this Court's "unitary business" cases, but intimates that such a conflict exists. *See* Pet. at 7-9. This suggestion is wrong. Examination of the cases referred to by petitioner makes clear that the state courts are engaging in the case-by-case, factual analysis mandated by this Court's decisions. Moreover, the results in these cases are entirely consistent with the decision of the Ohio Supreme Court below, illustrating that petitioner's real complaint is with the Ohio courts' factual finding that the investment funds were not used in AHP's other businesses.

First, petitioner cites *Sperry & Hutchinson Co. v. Department of Revenue*, 270 Or. 329, 527 P.2d 730 (1974), asserting that it supports taxation of the investment portion of AHP's funds. In fact, far from supporting the

petitioner's position, the result in *Sperry & Hutchinson* precisely tracks the result reached by the Ohio Supreme Court. The taxpayer in *Sperry & Hutchinson* divided its investment portfolio into three categories: short-term securities held as working capital; short-term securities held as investments; and long-term securities held as investments. The Oregon Supreme Court concluded that only the first category was subject to tax as part of the taxpayer's unitary business; the other two were not part of the taxpayer's unitary business and thus were not subject to the Oregon tax. Similarly, in this case the portion of AHP's funds used as working capital was considered subject to the Ohio tax, while the portion held for investment was deemed outside AHP's unitary business and thus not subject to the Ohio tax.

The second case petitioner cites, *Holiday Inns, Inc. v. Olsen*, 692 S.W.2d 850 (Tenn. 1985), also is completely consistent with the decision of the Ohio Supreme Court. In *Holiday Inns*, the Supreme Court of Tennessee concluded that "interest income from short-term investments of working capital" was taxable as part of the taxpayer's unitary business. *Id.* at 854. This result is precisely the same as the result here, since AHP's income from investment of working capital was deemed subject to tax in Ohio. It is the treatment of income from the investment of funds *not* held as working capital—an issue not presented in *Holiday Inns*—that petitioner seeks to have this Court review.

Third, petitioner cites *Silent Hoist & Crane Co. v. Director*, 100 N.J. 1, 494 A.2d 775, *cert. denied*, 474 U.S. 995 (1985). In *Silent Hoist*, the Court concluded that the investment activities of the taxpayer were closely related to the taxpayer's real estate and manufacturing businesses so as to form one integrated operation that was subject to tax as a unitary business. In reaching this decision, the *Silent Hoist* Court focused on several specific features of the taxpayer's operations, including its use of

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the investment funds as working capital for the other businesses, the integrated management of the three businesses, and the integrated financial and accounting treatment accorded to the businesses. *See* 100 N.J. at 20-21, 494 A.2d at 785. Here, in contrast, AHP's investment operations were conducted independently, and, as the Ohio Supreme Court carefully noted, were not used as a source of working capital for AHP's other businesses. *See* App. to Pet. at A-5. Thus, once again, the result in this case is completely consistent with the result reached by another state court.

Finally, petitioner cites *NCR Corp. v. Comptroller*, 313 Md. 118, 544 A.2d 764 (1988), and *M. Lowenstein Corp. v. South Carolina Tax Comm'n*, 298 S.C. 93, 378 S.E.2d 272 (1989), and briefly notes that each upholds the apportionment of investment income. In both, however, the investment income was used as working capital in the taxpayers' businesses. The Ohio courts, in contrast, have found that AHP's investment funds were not used as working capital or otherwise involved in AHP's business operations.

Thus, in every case in which investment funds were used as working capital in the taxpayer's business, the income from those funds was found to be subject to apportionment, just as the working capital portion of AHP's funds was apportioned here. In the two cases in which courts found investment funds were not used as working capital—*Sperry & Hutchinson* and this case—the income from those funds was held not to be subject to apportionment. Petitioner's attempt to develop a conflict from decisions so obviously in complete harmony exposes the true nature of petitioner's complaint. Petitioner simply refuses to accept the lower courts' finding that the investment portion of AHP's funds was not used in AHP's unitary business operations as a source of working capital. Review of this factual finding, however, is not an appropriate basis for a petition for certiorari.

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III. THE OHIO SUPREME COURT CORRECTLY APPLIED THIS COURT'S TEST OF A UNITARY BUSINESS

A petition for certiorari is an inappropriate stage for a full discussion of the merits of the unitary business determination by the Ohio Supreme Court. Petitioner has asserted, however, that review is warranted here solely because that determination was incorrect, so a short discussion of the merits is necessary. Even such a brief review demonstrates that the Ohio Supreme Court's decision was correct—it certainly meets the actual standard by falling " 'within the realm of permissible judgments.' " *Container Corp of America v. Franchise Tax Bd.*, 463 U.S. at 176 (footnote omitted). Petitioner's claimed error therefore is illusory and offers no basis for granting discretionary review.

As this Court has recognized, the application of the relevant constitutional standards is highly dependent on the particular facts presented: "the application of the unitary-business principle requires in each case a careful examination both of the way in which the corporate enterprise is structured and operates, and of the relationship with the taxing State." *ASARCO*, 458 U.S. at 326 n. 22. The Ohio Supreme Court conducted this type of a careful examination and found that the investment portion of AHP's funds had no connection with Ohio. Specifically, the Court noted that "the investment activity producing the income took place entirely outside Ohio and [that] the payors were discrete business entities." App. to Pet. at A-4. In addition, as noted earlier, the feature the Ohio Supreme Court found to be "pivotal" to its analysis was the factual finding that "AHP did not pledge the investments to secure loans of working capital and . . . did not require the funds directly for operational capital." *Id.* at A-7. These facts relied on by the Ohio Supreme Court were all based on findings of the Board of Tax Appeals, an essentially trial-level adjudicator that receives evidence and testimony.

On the basis of this particular factual record, the Ohio Supreme Court correctly applied the standards established by this Court. The two primary facts developed below both feature prominently in the appropriate constitutional analysis. First, the independent nature of AHP's New York investment activities establishes that they were not "related in some concrete way" to AHP's activities in Ohio, the relevant standard under this Court's decision in *Container Corp. of America v. Franchise Tax Bd.*, 463 U.S. at 166. In addition, in *ASARCO*, this Court made clear that a company's failure to use funds held for investment as a source of working capital indicates that the investment fund is outside the scope of the unitary business. *See* 458 U.S. at 324 n.21. The "pivotal" factual finding that AHP did not use the investment funds as a source of working capital therefore establishes that the income on those funds is non-unitary.

Thus, the petition should be denied, even if the inappropriateness of reviewing a mere factbound application of "well established" law, *id.* at 176, is overlooked. Because the Ohio Supreme Court's decision is correct, further review is not necessary.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted,

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